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**ENERGY DEREGULATION:  
ISSUES FACING NEW YORK**

*2001 Warren M. Anderson Legislative Breakfast Seminar Series*

**FEBRUARY 6, 2001**



Government Law Center  
Albany Law School | UNION UNIVERSITY

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**Hon. Maureen O. Helmer**

*New York State Public Service Commission*

**Barbara Brenner, Esq.**

*Couch White LLP*

**Gerald A. Norlander, Esq.**

*The Public Utility Law Project*

**Howard Shapiro, Esq.**

*The Energy Association of New York State, Inc.*

**Daniel B. Walsh**

*The Business Council of New York State, Inc.*

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**The 2001  
Warren M. Anderson  
Legislative Breakfast Seminar Series**

**ENERGY DEREGULATION:  
ISSUES FACING NEW YORK**

Transcript of the Panel Presentations  
Delivered at the Feb. 6, 2001, Seminar

2001 Legislative Session

The Assembly Parlor  
The Capitol  
Albany, N.Y.

**WARREN M. ANDERSON**

Warren M. Anderson is a distinguished alumnus of Albany Law School and an active member of the Government Law Center Advisory Board. Having served in the NYS Senate for thirty-five years, he is perhaps best known for his leadership during his tenure as President Pro Tem and Majority Leader from 1973 to 1988.

Warren Anderson began his legal career as an Assistant County Attorney in Broome County. He then joined the law firm of Hinman, Howard & Kattell where he is currently practicing law. Throughout his career he has received numerous honors and awards.

**PROGRAM DESCRIPTION**

In furtherance of its mission to serve as a resource to all levels of government in the resolution of specific problems, the Government Law Center is pleased to present the tenth annual Warren M. Anderson Legislative Breakfast Seminar Series. Monthly breakfast programs feature experts addressing the legal aspects of a variety of policy issues pending before the Legislature. The seminars are designed to provide access to current legal information on a given topic. The Government Law Center welcomes suggestions for future programs.

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## 2001 HONORARY CO-HOSTS

The Government Law Center is grateful to the Leadership of the New York State Senate and Assembly for serving as honorary co-hosts of the 2001 Series:

**Honorable Joseph L. Bruno**

*Senate Majority Leader*

**Honorable Sheldon Silver**

*Speaker of the NYS Assembly*

**Honorable Martin Connor**

*Senate Minority Leader*

**Honorable John Faso**

*Assembly Minority Leader*

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The Government Law Center would like to thank *Senator Joseph Bruno, Assemblyman Sheldon Silver, Senator Martin Connor, and Assemblyman John Faso* for serving as honorary co-hosts of The 2001 Anderson Series.

The Center also gratefully acknowledges the speakers who participated in the Feb. 6, 2001, program: *Hon. Maureen O. Helmer, Barbara Brenner, Esq., Gerald A. Norlander, Esq., Howard Shapiro, Esq., and Daniel B. Walsh.*

## TABLE OF CONTENTS

	<u>Page</u>
<b>Hon. Maureen O. Helmer</b> . . . . .	1
<i>Chairman, NYS Public Service Commission</i>	
<b>Barbara Brenner, Esq.</b> . . . . .	7
<i>Couch White LLP</i>	
<b>Gerald A. Norlander, Esq.</b> . . . . .	11
<i>Executive Director, The Public Utility Law Project</i>	
<b>Howard Shapiro, Esq.</b> . . . . .	17
<i>President and CEO, The Energy Association of New York State, Inc.</i>	
<b>Daniel B. Walsh</b> . . . . .	21
<i>President and CEO, The Business Council of New York State, Inc.</i>	

# HON. MAUREEN O. HELMER

Chairman

*NYS Public Service Commission*

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I would like to talk about California a little bit this morning. Some important differences exist between New York and California. California mandated that their utilities only buy on the spot market, the most volatile market. It has the most potential for price spikes and other problems. New York did not require its utilities to purchase through the spot market. Rather, it allowed them to essentially hedge; to have ongoing medium, short-term and some longer-term contracts, with divested generations, old IPPs, etc. That's been very important for New York. Even in Con Ed where the prices were relatively volatile last summer, only about half of their portfolio was on the spot market, providing a hedge last summer. By the way, it's our intention to provide even more of a hedge this summer given the rising gas prices. Another important issue is the dependance on imports from out of state. New York has most of the generation it needs right within the State. It has limited capability to take power from out of state. This can

be a weakness and we would like to strengthen the ability of New York to have commerce in and out of New York State. But for now, most of the generation New York needs is within New York State as opposed to California which is so dependent on out of State imports. Finally, and perhaps most importantly, New York did take a phased approach to deregulation. The early years did not expose all the customers to competition and market pricing. Frankly, we took it under the chin the first couple of years. The marketers were out there saying this would all be working if we had just done a flash cut to deregulation. As it turns out, and we can site California as an example, a flash cut probably is not the wise way to go.

What can we learn from California? First and foremost, the need for capacity. The need for capacity in California has been created by a growing economy that is more dependent than it was in the past on electricity. We're all familiar with the computers, server farms, and various other technology additions that every business and many homes now have come to enjoy. California's rate of growth for electric needs has actually outpaced the growing economy. The story is the same in New York. New York's economy has boomed and the State has sustained the economic growth that it has enjoyed for a longer period of time than anyone predicted. In 1996-97, the last State

energy master plan was developed. New York took a multi-agency approach to developing its energy policy. It projected the rate of economic growth and the increase in demand for electricity. There was a low, a moderate and a high forecast. We have outpaced the high forecast. Our peak in 1999 hit a high which was not predicted in the State Energy Plan. That high was not supposed to be hit until 2003. This gives you some sense of how quickly this has happened. We're now conducting the next round of the State Energy Plan and obviously these factors will be taken into consideration.

What does this say to New York? First of all, we need substantial new, clean and efficient electric generation. That's at the heart of the Article X siting process. The siting process got off to a slow start. The EPA, the federal agency which was responsible for delegating the federal permits to the DEC, sat on one letter for fourteen months. Then when they said we didn't have the appropriate delegation and the statute was changed, they sat on it for another year. That has held us up for three years. Having said that, the DEC and the PSC are now working very hard and increasingly well together to get these permits out the door. One was recently sited. Another was sited last year and the Army Corps is sitting on that. Four other plants, however, have gone through what's called the draft permit phase, a very

important phase where a lot of the work gets done. The period after that is usually shorter and more efficient.

We also have to look at the demand side. California did not develop an effective demand side market in time for this to work. There was not sufficient work done with their infrastructure (metering, tariffs and so forth) so that the buyers, especially the large customers, had the opportunity to make good economic decisions based on when electricity was priced the highest, when the demand was the highest, and when the peaks were the most severe. New York, in time for the summer, is putting in place a number of things including the availability of more advanced, competitive metering for larger customers. We're putting in place demand side tariffs so that customers have an ability, particularly in New York City, to have an impact on the market and the price of electricity in New York. We're also getting involved with the Independent System Operator (ISO). The ISO operates the grid, and implements the rules by which people bid into the grid, are dispatched into the grid, and so forth. There have been a number of issues with the ISO with respect to the rules that it applies to the open market. We're working with them particularly for the next summer to get in place things which would protect the consumer from severe price fights which are caused by market power. Right now, because our supply is just what

we need to meet our demand, there is an ability during certain hours of the year for certain participants to exert market power. We are working, therefore, with the ISO and all the market participants—the generators, the utilities, the customer groups, and the environmental groups—to develop something which will protect consumers during those most severe hours.

We are lucky to have the flexibility in New York to react to what happened in California. We have the ability to go back and make changes that are needed to the extent the customers are not as comfortable because of what's going on in California. We have the ability to respond, but our first priority is to move the competitive markets forward so that they work. California made a decision to just stop the clock in time. For those of you who remember back, in the Assembly if time ran out to debate at the end of the night, you just stopped the clock. California has just decided to stop the clock and, unfortunately, they stopped it at a very bad time. In New York, we want to move the clock forward and continue to develop these markets. At the same time, we want to recognize that there are genuine consumer issues that have to be dealt with during the transition.

Thank you for giving me the opportunity to speak here today.

## BARBARA BRENNER, ESQ.

### *Couch White LLP*

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It's important to recognize that the key issues facing New York today are not the result of deregulation. The most important issues are price and supply. First—price. The price was too high in New York before deregulation, and it is still above the national average. The main cause of the problem last summer was the spike in the price of natural gas. Without deregulation, consumers would have paid for that spike. Before deregulation, there was what was called a fuel adjustment clause and unexpected high fuel prices to generate electricity were passed through to consumers.

We have to bring the price of electricity down, but it is not deregulation that must go in order to do that. The only chance we have in the long run of bringing prices down is to have a robust competitive market. That is where we should all be focused. Higher rates and higher prices are a convenient excuse for people who feel that they do not want deregulation or they want to change the way it's being implemented in New York. I would agree with Chairman Helmer that we need to stay the course.

I think the single most important thing we can do is get new power plants sited as quickly as we possibly can. I don't think there's any other way to meet demand. We want businesses to locate in New York, we want homes and schools to have computers—and that takes electricity. Even though the demand side response is very important, without the power plants being built, we're not going to get there. It is important that people focus on this and to recognize that the lack of capacity is due to a robust economy. We don't want a recession and we don't want businesses to locate elsewhere. We want them here. They need to know that they will have electricity. You only have to read the newspapers and some of the comments out of the Silicone Valley to recognize that, even if there's only a perception that you may not have electricity in the future, that is taken into account by businesses in making location decisions.

It's important to recognize that the shortage of power plants would have occurred without deregulation. Don't blame deregulation for the shortage of capacity. "Blame" the robust economy in New York, especially downstate. Recognize that if the siting process takes too long, is too complicated, and is too difficult, the multinational corporations that are now thinking about investing in power plants in New York State have other places to invest. There are other States and other countries, and there are a limited

number of turbines that General Electric can turn out in any one year. Granted, many companies have proposed power plants here and New York is a desirable market. But, many of these companies have proposed power plants in other places. The first ones to get sited are the ones that are going to get the turbines.

There's nothing wrong with Article X. The law is well written, and has tried to accommodate the needs of all New Yorkers. What's wrong right now is the way that it is being implemented—it is simply taking too long. We need the federal government to cooperate with the state government. We need all the stakeholders to recognize that power plants are going to have to be built quickly or we're not going to have enough supply. If there's any opposition in the local communities or from other intervenors, it now takes as long as three years to get a power plant sited in New York State. It then takes at least another two years to build it. That means that power plants, except possibly the New York Power Authority peakers in New York City, are not going to be online even by the summer of 2003. Instead of people saying we should tweak this or change something else, we should focus on how are we going to get this process to work more effectively. We should all work on getting the local communities, the stakeholders, and the state and federal government to work together to get siting

to be implemented more quickly.

The policy debate over whether to have deregulation is not the debate we should be having now. We already have deregulation. The debate should be on whether we need to change things to make it work better. If we get power plants built, New York's infrastructure is fundamentally sound for the development of a robust competitive market. There are changes that need to be made in the rules. There is a process in place for doing that at the New York State Public Service Commission, the Federal Energy Regulatory Commission, and the New York State Independent System Operator. If I started to tell you the kind of changes that may be needed, your eyes would glaze over—no matter how much coffee you've had this morning. They are highly technical issues, not broad policy initiatives that can be addressed at a 30,000 foot level. We should leave the technical details to the technical people on the committees who know what the difference is between the day ahead market, the real time market, the ICAP market and all of the other electricity related markets that we're developing in New York.

Thank you.

# GERALD A. NORLANDER, ESQ.

Executive Director

## *The Public Utility Law Project*

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The events in California and in the Con Edison territory last summer are reframing dialogue on electric industry restructuring in the consumer movement around the country. The majority of the states, despite the cheerleading of the “RED Index,” have not gone far down the restructuring road, and those that began are dramatically slowing their pace. The debate is shifting to whether restructuring is a “big mistake” or a “bad idea.”

The “big mistake theory” is that a good idea, restructuring, was implemented incorrectly, and the wholesale market California relied upon was flawed. Similarly, it is argued that the New York Independent System Operator’s markets are flawed, but if we can just tweak them and improve them we can get market power out, and then they will work as intended to drive wholesale rates down.

The “bad idea theory” is that the poolco markets upon which divestiture and restructuring hinged haven’t

worked in England, they haven’t worked in Canada, and they haven’t worked in California. They’re not working in New York and they’re not likely to work anytime soon to create a reasonable wholesale market price for electricity that retail rate makers can rely upon in setting retail rates.

Today we have destabilized prices in the Con Edison territory and no one can tell you what the price will be next summer. This adversely affects households and businesses that are energy dependent. The New York ISO has suggested that if we have a hot summer and if grid conditions are not ideal, we may be faced with shortages. Yet there are no firm plans for Con Edison to create the adequate supply it is required to provide under our laws, and it’s uncertain who will be the next one who steps up to the plate to meet demand.

There is a market for stable priced electricity at predictable rates and reliable supply. Communities and states with stable rates are advertising that now and recruiting businesses to locate there. How many of you, if you were siting a new operation or expanded operation, would choose Los Angeles or New York City? That’s a trick question because Los Angeles did not deregulate. In Los Angeles, the utility owns its own power plants and has a surplus of generation. It doesn’t need to rely upon the wholesale markets. It has adequate supply, and it has a plan

for building new plants. The L.A. utility is repaying its debt by selling its energy surplus into the wild ISO markets, advertising its reliability by putting out news releases everyday, and stimulating articles about how the hot tubs are still bubbling; they haven't had a blackout, and they're helping to keep the lights on elsewhere, where the private sector utilities deregulated.

The proponents of electric restructuring offered New York consumers a new vision. It was a time of energy surpluses, and cheap energy was readily available in 1997. Expenditures on conservation measures could be reduced because the market would provide that, and we could rely upon the wholesale markets to supply cheap energy to customers who hadn't switched. If there was some volatility, the market would step forward and cure the problem by offering stable prices. That was the vision, but the reality today, five years later, is that there is no realistic choice for most customers except the very largest. We have in the Con Edison area particularly unstable spiking rates and some blackout possibilities.

The California experience deserves attention. There are at least three important lessons and three comparisons that I think we should make. I don't want to get into the issue of who is to blame for the problems. The first lesson is that generation has slipped over the line from state

regulation to federal regulation and the federal regulators are not setting just and reasonable rates. The ISO markets operating under federal jurisdiction have in California been found not to yield just and reasonable prices; yet the FERC has held that it lacks power to fix the prices. Their advice to the states is, "Why are you buying so much at our convenience store? Why don't you make bilateral contracts and so forth?" This was not the model offered in 1997, which was to create a liquid, transparent spot market and put as much of the energy as we could through it. New York very wisely did not encourage all its utilities to buy excessively on the spot market. Con Edison has gone down that road and is far too reliant on spot market purchases, like San Diego last summer. For now, the lesson is to rely as little on spot markets as we can.

Lesson two: We can control energy costs if we don't divest the generating plants. In this respect, Rochester and Los Angeles are comparable. Rochester Gas and Electric has not sold its plants, has frozen its energy prices at less than three cents, and has had no spikes or shortages. Similarly, the LA utility kept its power plants and has had no rate increases for nine years.

The third lesson is that retail price caps can work if the utilities hedge their risks. Compare NYSEG with the two California utilities on the verge of bankruptcy. All had

fixed retail prices; all divested or began to divest their generating plants. The difference is that the California utilities agreed to meet a future retail price without securing long term wholesale supply, placing themselves at the mercy of the volatile new spot market. In contrast, NYSE&G sold its plants, but its 8k statement says they've hedged their commodity risk. Thus, the company offers stable prices to consumers, unaffected by the volatility that harmed Con Edison's customers last summer. NYSE&G established a firm price that is known, residential customers can rely on it, and it's the price competitors have to beat.

New York is in a unique position because we never did deregulate—our laws are the same as before. There are interesting questions whether the new electric companies now certified to run the divested power plants have duties under state law to act in the public interest and serve customers in accordance with statutory requirements, including the provision of adequate service at reasonable rates.

For those who are interested, an expanded version of my remarks can be found at the Public Utility Law Project website ([http://www.pulp.tc/html/big\\_mistake.html](http://www.pulp.tc/html/big_mistake.html)).

Thank you.

## HOWARD SHAPIRO, ESQ.

President & CEO

*The Energy Association of New York State, Inc.*

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New York is not yet California. Our lights are on, we're all warm, and so far we don't have any energy emergencies. We need to pause as we look at this issue and realize that electricity and natural gas are very basic necessities. They're the lifeblood of our society, they're as important to our residential customers certainly as they are to our business customers. They are part of every facet of our life and in fact we've elevated our demand for electricity and natural gas to higher levels and insisted on higher and higher reliability. We are doing some things right in New York and it's no accident that New York has not experienced a California type crisis. A lot of that credit goes to the Public Service Commission and to its Chairman, Maureen Helmer, who has done an excellent job of managing the transition and avoiding a lot of the problems that have occurred elsewhere. We've also caught

some lucky breaks. We had the coolest summer in memory in New York City last year with not a single day over 90 degrees. That has certainly helped the reliability issues that the City was facing. We also don't have quite the population and the economic growth rates that California has experienced.

With all due respect to the title of this program, I think Barbara Brenner is exactly right. These issues that we are facing today here in New York are not about deregulation. The issue is one of additional supply. There still is the law of supply and demand and as someone recently said in a column I read, "The laws of economics are not optional." Our economy has grown faster than anyone anticipated just a few short years ago, and what has happened is that our infrastructure, our supply of electricity, has simply not kept up with that growing economy. That's the good news. We need additional supply for a number of reasons. We need to insure the crucial reliability that everybody has come to depend on and the increased level of reliability desired in a progressively technical world. We also need additional supply to create a downward pressure on prices and to facilitate, as Maureen said, the proper functioning of the wholesale market. We need to encourage existing companies to stay in New York and to expand in New York and for new companies to come to New York.

The one unsettling factor in comparisons of New York and California is that in neither state have we built additional supply in a number of years. Fortunately, as we are hearing this morning and elsewhere, the need for new generation is no longer subject to a serious debate. Virtually every single state leader and responsible elected official has said we need new generation facilities.

What I would like to focus on and leave with you all this morning is the way we solve that problem. We don't solve the problem by engaging in adversarial, contentious discussions as we often do in the Capitol. We solve the problem by rising above politics and agreeing to get things done. In this case the opportunity is enormous and the risks are, unfortunately, too serious to ignore. If we wait until the lights flicker, the game's over. It will be way too late. California made obvious mistakes and then Murphy's Law kicked in. Everything that could go wrong, did.

My basic message today is that we need statesmanship and strong political leadership. It's human nature to want our cake and to eat it to. We want ample supplies of cheap energy without having the additional infrastructure necessary to provide that energy. We talk about new generation and we talk about new supply. We also need the infrastructure that goes along with that new supply. We need additional gas supply. We need the

pipelines to bring in the gas. We need to maintain and enhance our transmission and distribution systems, which are still regulated by the Public Service Commission. We need to make sure we have enough capital to invest in those systems so that they can support the growing economy and the additional generation that we're building in this state. Barbara and I both represent companies that build power plants. The companies that I represent also distribute electricity and natural gas. They have choices when they decide to build power plants. They can invest their money in New York, in Pennsylvania, or Connecticut. As one told me yesterday, they can also invest in Brazil. If you were representing those companies and advising the management in terms of their responsibilities to their shareholders, where would you put your investments? That's a very serious question when we look at the time it takes to site a power plant in this state compared to neighboring states and other places in the world. It's also a very serious question when you ask a business person, "Where will you locate your business? Will you go to a state where they can build power plants and you'll have ample supply of electricity and natural gas, or will you go to a state where they can't tell when they're going to put the next power plant on line?" Those are the kinds of questions we're facing today and those are the issues that I think need to be resolved.

# DANIEL WALSH

President & CEO

*The Business Council of New York State, Inc.*

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New York State's energy markets have undergone significant changes in recent years. This is no longer a state that has seven investor-owned utilities. Under deregulation, most of these utilities have sold off their generating power and become "pipes-and-wires" companies responsible only for transmitting energy to customers. Some of these companies have the same name; others don't. For example, Niagara Mohawk is soon to be National Grid if regulators approve their proposed merger.

Changes in New York's energy markets go beyond questions about electricity. There are important issues related to supply and transmission of natural gas. The state in recent years has explored the value of alternative energy sources, such as windmills. And there are new state energy charges designed to encourage conservation. One of these, the systems benefit charge (SBC), is a surcharge on energy

bills that funds conservation programs and programs related to the exploration of alternative energy sources.

Of course conservation and alternative energy deserve our attention. I remember driving around Albany about a year and a half ago and seeing not one light on in the Capitol. Now, there are lights on in every building in this complex. There are reasons they were turned off—and there are reasons why they were brought back on.

Despite increased interest in conservation, there is little conservation in practice among most users. In our own lives and homes, we have many more electric gizmos than we used to. They range from the obvious like personal computers to less expected items that you use for things like brushing your teeth.

I know of no issue before the state Legislature or the Public Service Commission that is more serious than New York's energy situation. New York has legitimate concerns about the price and supply of energy, and if we don't address it, this state could become an economic wasteland. California is finding that out. There are already companies there, many of which have invested heavily in California in the past, that are now in dire trouble because of energy shortages. Many of these companies are considering making future job-creating investments in other states, where long-term energy supplies are more reliable.

The state Public Service Commission is doing a Herculean job managing the problem, but we are not out of the woods on energy issues. The state Legislature is considering a variety of bills to provide short-term relief. These efforts should be limited to the issues related to taxes; they should not, in our view, involve anything that would undermine or reverse the ongoing administrative process of deregulation.

But the political pressure on Albany will likely increase. For example, school districts, universities and similar large institutions are just beginning to grapple with the financial implications of the increased costs of heating and cooling their physical plants. There is even talk about introducing “real-time” metering residences, which would allow people to see the actual cost of electricity. This could dramatically change our everyday use of this reliable commodity.

Both state and federal lawmakers have to deal with this issue. Many of the most informed and involved individuals and institutions agree that New York needs more power plants soon and needs to expedite the siting of power plants. Most also recognize that New York’s energy markets, like any free and competitive market, will not function properly without adequate supplies to put downward pressure on prices. I think that business and environmental

interests can and should join government leaders at the table and negotiate a fair and reasonable path into a future with energy security for all New Yorkers.